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UNCLAS SECTION 01 OF 03 CAIRO 005350

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E.O. 12958: N/A
TAGS: ECON EFIN ETRD EINV EG
SUBJECT: UPDATE ON EGYPT'S PRIVATIZATION PROGRAM

REF: A. CAIRO 4374
¶B. CAIRO 1329

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Summary

¶1. (SBU) Since taking office in July 2004, Prime Minister Nazif's administration has reinvigorated the GOE's program to privatize state-owned industries. Under the leadership of the new Ministry of Investment, the revitalized program aims to speed up privatizations by making public enterprises more efficient - and thus more attractive to potential investors - while also introducing good corporate governance principles. The effort has paid off for the GOE, which completed a total of 19 privatizations from July 2004 to March 2005, generating LE 2.9 billion ($500 million) compared with five transactions generating LE 81 million ($14 million) in the period July 2003-March 2004. The GOE has promised even bolder steps in the near future for divestiture of formerly "strategic" industries. Labor issues remain a concern, but the GOE has indicated that it will deal with workers' concerns on a case-by-case basis as public companies are privatized. It is doubtful, however, that the GOE would approve any deals that would result in massive layoffs, particularly in an election year. End summary.

Privatization revitalized

¶2. (SBU) The GOE privatization program has undergone a complete makeover in concept and implementation in the last year under the Nazif administration's new Ministry of Investment (MOI). Minister of Investment Mahmoud Mohieldin has been the driving force behind revitalization of the program, which he refers to as "asset management." Mohieldin has used his political weight, as a key member of the NDP economic policy apparatus, to garner support for broadening the scope of the program to include all public enterprises, the more competitive companies as well as those with large workforces that could be negatively affected by privatization. He has made privatization a focal point of the macroeconomic reform effort led by the Minister of Finance, the Minister of Foreign Trade and Industry and Nazif himself, all of whom agree on the goals of stimulating private sector-driven growth and "marketing Egypt" as a destination for foreign investment.

Pre-Nazif: Privatization in fits and starts

¶3. (U) The GOE has two categories of public enterprises: wholly state-owned companies regulated by Law 203 of 1991, and joint venture companies (including banks) with a public-private ownership mix, regulated by Law 159 of 1981. When the privatization program began, the 314 wholly state-owned companies were grouped according to the type of economic activity they conducted and put under the supervision of holding companies (HCs). The HCs managed the privatization of their affiliate companies, eventually dissolving when all of their affiliates had been privatized. This process created a conflict of interest, especially for the HC chairmen. Working efficiently to privatize all of their affiliates meant that the HC chairmen worked themselves out of a job. Privatization was therefore a slow, sporadic process and after more than a decade of fits and starts, liquidations and restructuring, there were still seven HCs with 139 affiliate companies.

¶4. (U) In 1999, after a cabinet change, the GOE decided to include the sale of public shares in joint venture companies under the rubric of the privatization program. The Ministry of Economy and Foreign Trade (now the Ministry of Foreign

Trade and Industry) began an inventory of joint ventures and their shareholder structure. After a lengthy research process, the number of joint venture companies and banks was found to exceed 600, all with different percentages of public ownership. In early 2000, the entire privatization program, including wholly state owned companies and joint ventures, was consolidated under the Ministry of Public Enterprises, where it remain until being subsumed by the new MOI in the July 2004 cabinet change.

Privatization under Nazif

¶5. (U) Soon after MOI took over managing the privatization program, a three-pronged effort was undertaken to remake public enterprises by: 1) restructuring and re-engineering public companies to make them more efficient, and ultimately more attractive to potential purchasers; 2) implementing good corporate governance principles in all public companies; and 3) aggressively pursuing the advertisement and sale of public companies. As part of the effort to introduce corporate governance principles, MOI published an OECD-based code of conduct for corporate governance and disclosure in public companies and began publishing the minutes of companies' general assembly meetings to increase transparency. MOI also created a ministerial committee to assist investors in resolving disputes arising from privatization transactions. The committee has already reportedly resolved 18 disputes, including several long-standing disputes from privatizations that occurred in the pre-Nazif era.

¶6. (U) MOI also began a campaign to advertise the newly revamped privatization program. The thrust of the ad campaign was that the GOE was committed to removing obstacles that had blocked or slowed privatizations in the past. Labor and debt issues would be dealt with on a case-by-case basis, foreign private sector interest was encouraged rather than feared as it had been under previous administrations, and no sectors were off-limits or "strategic" as in the past. On behalf of MOI, Microsoft Chairman Bill Gates launched a website, www.investment.gov.eg in January 2005, to serve as Egypt's investment portal. The GOE then took its investment campaign to the May 2005 World Economic Forum in an effort to drum up more foreign investment.

¶7. (U) The result of MOI's efforts has been a rekindling of interest among foreign investors. A list of 41 local and international financial institutions, including Citibank, Goldman Sachs and Merrill Lynch, are now working with MOI as advisors/consultants on privatization. A number of prominent foreign companies - such as Ciments Francais, La Farge Titan and Michelin - concluded multi-million dollar deals to purchase public companies such as Suez Cement (ref B). From July 2004 to March 2005, the GOE completed 19 privatizations, generating LE 2.9 billion in revenue, compared with only five transactions that generated LE 81 million in the period July 2003-March 2004. MOI expects the total value of privatizations in fiscal year 2004/2005 to exceed LE 3 billion, almost double the aggregate value of sales for the period 2001 through June 2004. The budget for fiscal year 2005/2006 (July 2005-June 2006) projects revenues from privatization will reach LE 5 billion (ref A).

Privatization expanded

¶8. (U) As noted above, MOI has included in the privatization program companies that were not previously slated for sale. Prior administrations considered certain companies "cash cows" that were too valuable for the GOE to sell. Likewise, certain sectors, such as petrochemicals and telecoms, were considered "strategic" and therefore off limits to private ownership, especially foreign private ownership. In June MOI sold 20% of the GOE's stake in Sidi Krir petrochemical company on the Cairo and Alexandria Stock Exchange (CASE) for LE 70/share. The company's shares have dominated trading by volume and value on the CASE in the last several weeks and recently closed at LE 105/share. A number of other high profile companies are also in the pipeline, including petroleum company AMOC and Eastern Tobacco Company (one of the GOE's "cash cows"). MOI has also indicated it will offer a significant stake in Telecom Egypt by the end of 2005. Shares of several public companies, possibly including Telecom Egypt, will also soon be registered on the New York Stock Exchange to further open channels for foreign investment. (Note: An update on privatization in the banking sector will be sent septel. End note).

Labor issues

¶10. (SBU) One of the difficult issues for the GOE as it divests its public assets is the reaction of labor. The GOE deals with excess labor in companies to be privatized by offering early retirement packages, which are largely funded by proceeds from privatization. Senior GOE officials continue to provide public reassurances that labor issues will be resolved amicably and a safety net will be provided for workers affected by privatization, in keeping with the GOE's general policy of protection of low-income earners. The MOI is working on a new early retirement system designed to more closely address workers' concerns and improve the financial management of privatization proceeds that will be used to fund the early retirements.

¶11. (SBU) Nevertheless, in state-owned enterprises, particularly those burdened with surplus manpower like textiles, iron, and steel, concerned workers have expressed opposition to privatization through their representatives in parliament, through strikes and in the opposition press. The proposed sale of shares in Suez and Torah Cement Companies late last year triggered strikes that were resolved only after MOI obtained the purchaser's commitment not to lay off workers for three years (ref B). Mohamed Hassouna, Advisor to the Minister on Privatization Affairs, told Econoff that MOI is "keeping channels open to workers," and cooperating with the Egyptian Trade Union Federation (ETUF) on a case-by-case basis to resolve potential problems with privatization deals. It would be surprising, however, for the GOE to conclude any deals that risk large-scale layoffs from labor-intensive industries prior to Egypt's October elections.

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